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No. 06-1620

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SUPREME COURT, U.S.

In The

Supreme Court of the United States

STEPHEN MARTIN and SUSAN MARTIN,

Petitioners,

v.

SANDERSON FARMS, INC., JAMES STUDENSKY, and FARMERS STATE BANK,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

BRIEF FOR RESPONDENT FARMERS STATE BANK IN OPPOSITION

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QUESTION PRESENTED

1. Certified Fed. R. App. P. 44(a) and (b) challenges that raise a single question are presented:

   Whether 28 U.S.C. §§ 151, 157, 1334 (made bankruptcy courts units of the Federal District Courts); the Federal Arbitration Act (FAA) and the Texas General Arbitration Act (TGAA); and Article V of the Texas Constitution – are all similarly unconstitutional in that Congress lacks constitutional authority to confer Article III powers on judges who lack the life tenure and salary security of Article III judges.

RULE 29.6 STATEMENT

Farmers State Bank is wholly owned by Farmers Delaware Bancshares, Inc., a Delaware corporation, which Delaware corporation is wholly owned by Farmers Bancshares, Inc., a Texas corporation. Farmers State Bank is located in Center, Texas.

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BRIEF FOR RESPONDENT FARMERS STATE BANK IN OPPOSITION

STATEMENT OF FACTS

The Petitioners, Steve and Susan Martin, sued Sanderson Farms, Inc. and Farmers State Bank in a Texas state court. The cause of action against Farmers and Sanderson arose from a series of agreements whereby the Martins agreed to construct egg hatching barns for Sanderson with financing from Farmers. Sanderson moved to compel arbitration of all of the Martins' claims against it based upon the arbitration clause in their agreement. The court granted Sanderson's motion and abated the case pending the completion of binding arbitration. The parties did not complete the arbitration because the cost was too high for the Martins. The Martins voluntarily nonsuited their state court case against both Sanderson and Farmers in March of 2003.

In July of 2003, the Martins voluntarily filed a Chapter 7 bankruptcy in federal court for the Western District of Texas and were granted a discharge in October of 2003. The Martins' creditors included Farmers and Sanderson. On their bankruptcy schedules, the Martins listed a cause of action against "Sanderson and/or Farmers State Bank" that they initially valued at zero but later amended to be an "unknown" value. The Martins failed to claim this cause of action as exempt property. This cause of action was based upon the same transactions as the Martins' case in the state court.

The trustee for the bankruptcy estate reached a compromise of this cause of action with both Sanderson and Farmers for $5,000.00 each. In 2004, the trustee moved the bankruptcy court for approval of these compromises. After a

hearing and thoughtful consideration, the court approved the compromise with Farmers and the compromise with Sanderson. The bankruptcy judge's approval of the compromise with Farmers was upheld by the district court and the Fifth Circuit Court of Appeals. The approval of the compromise with Sanderson is pending in the bankruptcy court for the correction of a minor factual error.

The Martins now complain that state and federal laws permitting binding arbitration and the "lack of life tenure and salary security" of not only the bankruptcy judge but also Texas state judges and arbitrators deprived the Martins of constitutionally protected rights. The Martins raised these issues for the first time before the Fifth Circuit Court of Appeals.

REASONS FOR DENYING THE PETITION

1. The Martins failed to preserve for appeal the constitutional issues they argue to this Court.

The Martins argue to this Court that certain provisions of the current bankruptcy law, the "Federal Arbitration Act," the "Texas General Arbitration Act," and Article V of the Texas Constitution are all unconstitutional. However, they neglected to raise any of these issues before the bankruptcy court or the district court. Outside of exceptional cases, it is the settled practice of this Court to

consider on appeal only those questions addressed in the lower courts.[1] This is not an exceptional case.

The Martins also failed to include these issues in the notice of appeal required by Bankruptcy Rule 8006 and so failed to preserve them for appeal.[2] Because of this failing, the Fifth Circuit did not address them. Since these constitutional issues are the only ones listed in the Martins' "Question Presented" on page i of their Petition and they were not preserved for appeal or addressed by the lower courts, the Martins' Petition should be denied.

2. The Martins erroneously believe that the cause of action against Farmers belongs to them and not to the bankruptcy estate and they base their arguments upon this belief.

In their Petition for Review, the Martins claim that two federal acts, one Texas act, and a provision of the Texas Constitution are all unconstitutional because, according to them, these laws prevented them from presenting their cause of action against Farmers to a jury or to a "qualified" judge. The unstated and erroneous premise that underlies the majority of their arguments is that they – the Martins – not the bankruptcy estate, own this cause of action against Farmers.

The Martins failed in two separate ways to maintain ownership or control over the cause of action they alleged

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[1] *McGoldrick v. Compagnie Generale Transatlantique*, 309 U.S. 430, 434 (1940) citing *Blair v. Oesterlein Co.*, 275 U.S. 220, 225 (1927); *Duignan v. United States*, 274 U.S. 195, 200 (1927).

[2] *In re GGM, P.C.*, 165 F.3d 1026, 1032 (5th Cir. 1999).

against Farmers when they filed for Chapter 7 bankruptcy. First, the Martins failed to list this cause of action as exempt property on their bankruptcy schedules. They listed this asset on Schedule B – Personal Property – not Schedule C – Property Claimed as Exempt. They did not contest the findings of the Fifth Circuit, the district court, or the bankruptcy court that this cause of action was not listed as exempt property.

Second, they claimed the personal property exemptions allowed to them under Texas state law in their bankruptcy filings. Availing themselves of these exemptions precluded them from characterizing their cause of action against Farmers as exempt property.[3] Since the cause of action against Farmers was not exempt property, it became the property of the bankruptcy estate to be used to satisfy creditors of the estate if possible and ceased to be the Martins' property. "It is true that if a cause of action *belongs* to the estate, then the trustee has exclusive standing to assert the claim."[4] The Martins had no standing to control when, how, or if the claim against Farmers was used once that claim became the property of the bankruptcy estate. The Martins simply do not understand this basic fact and their contentions that their constitutional rights have been abridged flow from this misunderstanding.

The Martins argue that the bankruptcy court did not have the authority to approve the trustee's compromise of

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[3] § 42.002 TEX. PROP. CODE (Lexis 2007)

[4] *In re Porras*, 312 B.R. 81, 94 (Bankr. W.D. Tex. 2004) (citing *In re Educators Group Health Trust*, 25 F.3d 1281, 1284 (5th Cir. 1994) and *In re S.I. Acquisition, Inc. v. Eastway Delivery Service, Inc. (S.I. Acquisition, Inc.)*, 817 F.2d 1142, 1153 (5th Cir. 1987).

the cause of action against Farmers for two reasons. First, because the cause of action belonged to them and was an exempt asset. As explained above, this is simply wrong. Second, because the cause of action was an "imaginary controversy". As near as Farmers can tell, this is sort of a "ripeness" argument and so is inapplicable as a basis to deny the parties involved the opportunity to settle it if they so desired. If the Martins indeed believed the cause of action against Farmers was an "imaginary controversy," why did they list it on their bankruptcy schedule as an asset?

3. The Fifth Circuit was right about the standard of review to be employed when considering the bankruptcy court's decision to approve a compromise of a bankruptcy estate's cause of action against a creditor of the estate.

The Martins claim that the Fifth Circuit should have reviewed *de novo* the bankruptcy court's decision to approve the trustee's compromise of the cause of action against Farmers. The Martins are wrong. Bankruptcy Rule 9019 gives the bankruptcy court the authority to approve a compromise of a bankruptcy estate's claim.[5] When reviewing a bankruptcy court's decision to approve or disapprove a compromise under this Rule, an appellate

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[5] "Rule 9019. Compromise and Arbitration (a) Compromise. On motion by the trustee and after notice and a hearing, the court may approve a compromise or settlement. Notice shall be given to creditors, the United States trustee, the debtor, and indenture trustees as provided in Rule 2002 and to any other entity as the court may direct." Fed. R. Bankr. P. 9019 (Lexis 2007). The Advisory Committee Notes state that Subdivision (a) of this rule is essentially the same as the provisions of former Bankruptcy Rule 191.

court utilizes an abuse of discretion standard.[6] It does not engage in a *de novo* review. The Fifth Circuit upheld the bankruptcy court's approval of the trustee's compromise with Farmers because it correctly found that the bankruptcy judge did not abuse his discretion. The bankruptcy court engaged in a thorough and careful review of the facts using the factors enumerated in *In re Jackson Brewing Co.* and, finding the compromise to be in the best interest of the estate, decided to approve it.[7]

4. The provisions of the "Bankruptcy Amendments and Federal Judgeship Act of 1984," 28 U.S.C.S. § 151 *et seq.*, are constitutional.

The Martins make the same arguments about the current bankruptcy laws that were made about the 1978 bankruptcy laws in *N. Pipeline Constr. Co. v. Marathon Pipe Line Co.* back in 1982.[8] In *Northern Pipeline* the Supreme Court held that the "jurisdictional provision of the 1978 Bankruptcy Reform Act unconstitutionally delegated Article III judicial authority and power to the bankruptcy courts."[9] Congress' revision of the bankruptcy laws in the "Bankruptcy Amendments and Federal Judgeship Act of

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[6] *In re the Matter of AWECO, Inc.*, 725 F.2d 293, 297 (5th Cir. 1984) *cert. denied* 469 U.S. 880 (1984) citing *In re Jackson Brewing Co.*, 624 F.2d 599, 602-603 (5th Cir. 1980); *Matter of Walsh Const.*, 669 F.2d 1325, 1328 (9th Cir. 1982); *Matter of Ocobock*, 608 F.2d 1358, 1360 (10th Cir. 1979); *In re Albert Harris*, 313 F.2d 447, 449 (6th Cir. 1963).

[7] *In re Jackson Brewing Co.*, 624 F.2d 599, 602-603 (5th Cir. 1980).

[8] *N. Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982).

[9] *In re Case*, 937 F.2d 1014, 1019 (5th Cir. 1991).

1984," 28 U.S.C.S. § 151 *et seq.*, modeled after the *Northern Pipeline* decision corrected this problem. Under the current law, a bankruptcy judge can only fully adjudicate a "core" proceeding as that is defined in non-exclusive terms in Section 157(b)(2).[10] With respect to "non-core" proceedings that are related to a bankruptcy case, a bankruptcy judge is restricted to conducting a preliminary hearing and submitting proposed findings of fact and conclusions of law to the district judge. Only the district judge may enter a final order or judgment.[11] If a party objects to the bankruptcy judge's findings or conclusions, they are reviewed *de novo* by the district judge.[12] This system has been found to be constitutional by numerous courts.[13] The Martins fail to explain how the changes made to the bankruptcy laws by Congress in the wake of *Northern Pipeline* fail to meet the requirements of Article III.

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[10] 28 U.S.C.S. § 157(b)(2) (Lexis 2007).

[11] 28 U.S.C.S. § 157(c) (Lexis 2007).

[12] Id.

[13] *In re Production Steel Inc.*, 48 B.R. 841 (M.D. Tenn. 1985); *In re Tom Carter Enterprises, Inc.*, 44 B.R. 605 (C.D. Cal. 1984); *In re WWG Industries*, 44 B.R. 287 (N.D. Ga. 1984); *In re Earle Industries, Inc.*, 71 B.R. 919 (Bankr. E.D. Pa. 1987); *In re Stephen W. Grosse*, P.C., 84 B.R. 377 (Bankr. D. Pa. 1988); *Carlton v. BAWW, Inc.*, 751 F.2d 781 (5th Cir. 1985); *Pate v. Hunt*, 136 B.R. 437 (Bankr. D. Tex. 1991); *In re Chase & Sanborn Corp.*, 51 B.R. 733 (Bankr. S.D. Fla. 1985); *In re Northwest Cinema Corp.*, 49 B.R. 479 (Bankr. E.D. Minn. 1985); *Storage Equities, Inc. v. Delisle*, 91 B.R. 616 (D. Ga. 1988); and *In re Lathrop*, 49 B.R. 885 (Bankr. D. Ill. 1985).

5. The Martins present no coherent basis for their claim that the "Federal Arbitration Act," the "Texas General Arbitration Act," or Article V of the Texas Constitution are unconstitutional.

Before filing for bankruptcy, the Martins sued Farmers and Sanderson in Texas state court. The state court ordered the Martins and Sanderson to participate in binding arbitration based upon the arbitration clause in their agreement. The cost of the arbitration proved too great so the Martins did not arbitrate their claims and instead nonsuited their case against both Farmers and Sanderson. The Martins never re-filed in state court. They did not get their jury trial. The Martins then filed for bankruptcy protection which, as explained above, caused the ownership of this cause of action against Farmers and Sanderson to change from the Martins to the bankruptcy estate.

The Martins argue that the "Federal Arbitration Act" and the "Texas General Arbitration Act" as well as Article V of the Texas Constitution are all unconstitutional because, according to them, these laws vest Texas judges and arbitrators with the same powers as federal Article III judges but fail to provide the Article III safeguards of life-tenure and salary security.

This argument is flawed for many reasons. First, the Martins ignore the fact that the state court judge did not order them to arbitrate their case against Farmers. The order applied only to the Martins and Sanderson. The Martins fail to show any impediment that prevented them from pursuing their claim in state court against Farmers. Second, the Martins also ignore the fact that neither the federal nor the Texas state arbitration act compels a party to present their case to an arbitrator instead of a judge.

Both Acts require that a party affirmatively choose arbitration in a contract or other written statement.[14] Third, in the interest of comity, this Court should not accept the Martins' request to pass upon the constitutionality of a Texas state statute or constitutional provision when no Texas state court has even had the opportunity to consider the Martin's argument. Fourth, Article III of the U.S. Constitution addresses the federal judiciary not the judiciary of the several states so Texas is under no constitutional obligation to adhere to these requirements.[15] And, Article III does not address or apply to arbitrators. Finally, since the Martins feel that their rights were infringed by the state court's decision that the contract they signed required them to arbitrate their case against Sanderson, the proper course of action would have been to appeal the state trial court's decision to a Texas appellate court. They failed to do this.

CONCLUSION

The Martins failed to preserve for appeal any of the constitutional arguments they make to this Court. They failed to present this Court with any coherent arguments in support of their claims that the "Bankruptcy Amendments and Federal Judgeship Act of 1984," the "Federal Arbitration Act," the "Texas General Arbitration Act," or Article V of the Texas Constitution are unconstitutional. None of the lower courts committed any error in this

[14] 9 U.S.C.S. §§ 2, 4 (Lexis 2007) and TEX. CIV. PRAC. & REM. CODE § 171.001 (Lexis 2007).

[15] U.S. CONST. amend. X.

matter. There is no conflict between the circuit courts as to any decisions made by the Fifth Circuit in this matter. And, there is no compelling reason to grant the Martins' Petition for Writ of Certiorari. The Petition for Writ of Certiorari should be denied.

Respectfully submitted,

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